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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Debtor.	Adv. Pro. No. 08-01789 (SMB) SIPA LIQUIDATION (Substantively Consolidated)
IRVING H. PICARD, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC, Plaintiff, v. HSBC BANK PLC, et al., Defendants.	Adv. Pro. No. 09-01364 (SMB)

TRUSTEE'S MEMORANDUM OF LAW IN OPPOSITION TO ALPHA PRIME FUND LTD.'S AND SENATOR FUND SPC'S MOTION FOR AN ORDER PURSUANT TO SECTION 105(a) OF THE BANKRUPTCY CODE AND GENERAL ORDER M-390 AUTHORIZING ALTERNATIVE DISPUTE RESOLUTION PROCEDURES

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Rules

Other Authorities

Irving H. Picard, as trustee (the "Trustee") for the substantively consolidated liquidation of the business of Bernard L. Madoff Investment Securities LLC ("BLMIS") under the Securities Investor Protection Act, 15 U.S.C. § 78aaa *et seq.* ("SIPA"), and the estate of Bernard L. Madoff ("Madoff"), respectfully submits this memorandum of law in opposition to defendants Alpha Prime Fund Limited's ("Alpha Prime") and Senator Fund SPC's ("Senator Fund") motion for an order pursuant to section 105(a) of the Bankruptcy Code and General Order M-390 Authorizing Alternative Dispute Resolution Procedures (the "Motion").

PRELIMINARY STATEMENT

Complaining of the pace of litigation—which, in this case, has been delayed by their own recalcitrance and litigation tactics—Alpha Prime and Senator Fund seek to strong-arm the Trustee into sitting with them at the negotiating table again, just months after the latest in their series of settlement discussions with the Trustee failed, and with the circumstances unchanged since then. It is not the parties' unwillingness to negotiate that has derailed past discussions—several times over the past four and a half years, the Trustee has engaged directly with Alpha Prime and Senator Fund about possible settlement. Nor is it an inability to find a structure within which to negotiate—the parties agreed to such a structure. Rather, it is the moving defendants' conduct that made past negotiations unsuccessful and make mediation at this time likely to fail, resulting only in the waste of party resources. Regardless of whether the Motion would be proper under any circumstances, given the circumstances here, the Motion should be denied.

The Motion puts the Trustee in the unfortunate position of having to allude to settlement discussions to oppose the Motion, yet protect the substance of the discussions pursuant to Rule

408 of the Federal Rules of Evidence.[1] Nevertheless, the tenor of the discussions demonstrates why the Trustee opposes the Motion. In 2013, as part of a settlement discussion, Alpha Prime provided voluntary "disclosures" that omitted potentially inculpatory materials. When the Trustee asked Alpha Prime to address those omissions by producing documents, the fund first skirted the issue and then resorted to clumsy brinksmanship, including "requesting" the information in the Trustee's possession so that it could withhold information and tailor its disclosures to match the third-party materials already in the Trustee's possession. Now, in the guise of streamlining and efficiency, the funds say that the claims should be mediated without exchanging any further evidence with the Trustee before mediation, but that they should be free to submit evidence to a mediator to demonstrate their purported good faith.

The chances of any meditation's success are tied to the parties' willingness to participate in good faith and exchange information related to the merits of the claim. Here, the funds have made clear that they are unwilling to disclose facts concerning the circumstances in which they received transfers from BLMIS—the facts at the heart of the Trustee's claims to avoid and recover customer property from the funds and the Trustee's claims to subordinate the funds' customer claims. While in general, the early, amicable resolution of claims may benefit the BLMIS customer property estate, here, in light of the parties' past negotiations and the funds' positions in the Motion, mediation will likely only result in further waste. The funds should not be permitted to strong-arm the Trustee to engage in mediation.

[1] The substance of all settlement discussions referred to in this memorandum of law is subject to Fed. R. Evid. 408, and therefore is not disclosed herein.

STATEMENT OF FACTS

I. THE TRUSTEE'S ACTIONS AGAINST ALPHA PRIME AND SENATOR FUND

Alpha Prime and Senator Fund were investment vehicles solely invested in BLMIS. The two funds have similar origins, both having been co-founded by Ursula Radel-Leszczynski, with the backing of Bank Medici, both defendants here.[2] The funds were operated by officers and directors, some of whom were involved with both funds.[3] Despite those commonalities, each fund's investment history with BLMIS is independent of the other's, and each fund engaged in separate conduct with respect to the customer property it received.

Alpha Prime held a BLMIS account from June 2003 through December 2008 and, in that time, received avoidable transfers totaling $85,824,714.[4] Senator Fund held a BLMIS account from July 2006 through December 2008, and in that time, received transfers totaling $95,392,688.[5]

The Trustee sued Alpha Prime and, later, Senator Fund for the avoidance and recovery of preferential and fraudulent transfers, and the disallowance or subordination of their customer claims.

Alpha Prime has employed diversionary tactics from the beginning of this litigation. Although typically treated as a tagalong in discussions between Alpha Prime and the Trustee—and sometimes not present at all—Senator Fund's dealings with the Trustee have been

[2] *See* Am. Compl. at 28–29, ECF No. 34.

[3] *Id.*

[4] *Id.* at 117.

[5] *Id.* at 118.

characterized by similar gamesmanship. In July 2009, the Trustee filed a complaint, seeking to avoid and recover the preferential and fraudulent transfers Alpha Prime received, and to disallow its customer claim. Alpha Prime was served with the complaint in July 2009, but did not timely respond or seek an extension of the deadline by which to respond. Instead, after contacting the Trustee to initiate settlement discussions, it chose to remain in default, backing out of an agreement with the Trustee to accept service of the complaint in exchange for the vacation of the default,[6] on the mistaken belief that by remaining in default, the fund would avoid the jurisdiction of the Bankruptcy Court.

In May 2010, Alpha Prime renewed its efforts to settle with the Trustee. This time, although not yet a defendant in any case commenced by the Trustee, Senator Fund entered the discussions as well. The primary reason the two funds approached the Trustee to discuss settlement together appears not to be to resolve issues involving factual commonalities, but rather because they are represented by the same counsel. The discussions were not fruitful.

On December 5, 2010, with the benefit of the Rule 2004 investigation, the Trustee filed an amended complaint in the Alpha Prime case. In the amended complaint, the Trustee named not only Alpha Prime, but Senator Fund and over sixty other parties as defendants. Each defendant named in the amended complaint is either a Madoff feeder fund serviced by an HSBC Bank entity, an agent (mainly directors and service providers) of the defendant feeder funds, or an HSBC Bank entity. In the amended complaint, the Trustee alleged that the defendants, having observed that various claims Madoff made about his trading were impossible and having

[6] In September 2010, in exchange for granting its consent to the Trustee's filing of an amended complaint, Alpha Prime's default was vacated. *See* Stipulation and Order (i) Vacating Entry of Default and (ii) Permitting the Trustee to File an Amended Complaint, ECF No. 27.

understood Madoff's representations to be indicia of fraud, were aware of the fraud. Those allegations support the Trustee's causes of action against Alpha Prime—the avoidance and recovery of the transfers of customer property under SIPA and the Bankruptcy Code and the disallowance or subordination of its customer claim. The Trustee asserted similar causes of action against Senator Fund, supported by similar factual allegations. The Trustee's avoidance and subordination claims are fact-intensive, and any settlement discussion or mediation of those claims will necessarily involve those facts.

II. ALPHA PRIME'S, SENATOR FUND'S, AND THEIR SERVICE PROVIDERS' LITIGATION TACTICS IN THE HSBC ACTION

In the Motion, Alpha Prime and Senator Fund complain that litigation has not progressed quickly enough to satisfy them, and therefore, the Trustee must be compelled to mediation. But the funds' tactics, and the tactics of affiliated parties represented by the same counsel, are the cause of the delay in the case.

Counsel for Alpha Prime and Senator Fund also represents several of the service provider defendants named in the case, including Alpha Prime Asset Management and Tereo Trust, Alpha Prime's investment manager and investment adviser, and Regulus Asset Management and Carruba Asset Management, Senator Fund's investment manager and investment adviser.[7] Although those parties are not before the Court on the Motion, their conduct is relevant because they employed several similar tactics, including a misguided attempt to strong-arm the Trustee to participate in mediation.

[7] The same counsel also represents defendant Ursula Radel-Leszczynski, a co-founder and former director of both Alpha Prime and Senator Fund, and White Orchard Investments Ltd., a defendant in another adversary proceeding, which has been in default for nearly two years.

In December 2011, Alpha Prime Asset Management, Carruba, and Regulus moved to dismiss the Trustee's claims for lack of personal jurisdiction. Tereo moved to dismiss for failure to state a claim. After the motions were fully briefed, the parties stipulated to engage in limited jurisdictional discovery. The four moving defendants made an initial production of documents that, in light of documents the Trustee had received from other parties in the Rule 2004 investigation, was clearly incomplete. The four moving defendants omitted from their production documents demonstrating the parties' jurisdictionally relevant contacts, including documents that were unquestionably in their possession. The Trustee asked for confirmation that the production was the entirety of the documents the defendants intended to produce. The defendants delayed in responding. The Trustee spent the next ten weeks fighting through a series of diversions, receiving no further documents, before these defendants demanded that the Trustee submit to mediation instead of continuing to litigate the motions to dismiss. Mediation was then, as it is now, an inappropriate method of proceeding, given the defendants' obstruction of the discovery process in the face of the litigation of fact-sensitive issues.

Within a few weeks, perhaps sensing a stalemate and in light of communications with the court, the defendants claimed to have suddenly gained access to additional documents. One day later, although not authorized by the stipulation or the Federal Rules of Civil Procedure, the defendants served a request for production of documents and interrogatories on the Trustee. The stated goal behind this request was to allow these defendants to provide back to the Trustee only the documents that the Trustee already had in his possession.

The Trustee pointed out that by serving the discovery requests, the defendants had submitted to jurisdiction and that, in any event, the Trustee refused to respond, because doing so would allow the defendants to omit any additional inculpatory material from their responses.

Three weeks later, the defendants withdrew their motions, and three months after that, the defendants filed answers to the Trustee's complaint.

The funds themselves have also contributed to the protracted litigation of legal issues for which they sought the withdrawal of the Bankruptcy Court reference. In May 2011, Alpha Prime and Senator Fund filed a joint answer and cross-claim against HSBC. Nonetheless, in September 2011, the funds joined the motion filed by another defendant feeder fund seeking the withdrawal of the Bankruptcy Court reference so that the District Court could consider: (1) the "safe harbor" defense under section 546(e) of the Bankruptcy Code (even though Senator Fund received transfers only within the two-year period); and (2) the standard for an avoidance claim under sections548(a)(1)(A), 548(c), and 550(b) of the Bankruptcy Code, even though they had already answered the complaint.

In connection with the second issue, in July 2012, Alpha Prime and Senator Fund, as joint lead defendants, filed a consolidated brief on behalf of BLMIS customers to challenge the "good faith" standard as it applies to avoidance actions pursuant to 11 U.S.C. § 548(c) or 11 U.S.C. § 550(b) in SIPA cases. Although they had already submitted the main brief on the issue, Alpha Prime and Senator also jointly signed one of the supplemental briefs on the same issue. The issues raised in those briefs have not yet been decided by the District Court, and thus remain pending. Thus, when Alpha Prime and Senator Fund complain that this action has taken too long, they should look to their litigation decisions: Alpha Prime was in default for over a year; both defendants requested extensions to respond to the complaint, and both filed motions shortly after filing answers, depriving the Trustee the ability to move the case forward.

In late 2012, Alpha Prime and Senator Fund sought to rekindle settlement discussions with the Trustee. Recognizing that for settlement discussions to advance, the Trustee would

need certain facts, the funds' counsel proposed that each fund enter into a term sheet with the Trustee governing, among other things, voluntary disclosure. The Trustee and Alpha Prime executed a term sheet. Senator Fund, however, did not enter into a term sheet.

From the start, Alpha Prime's disclosure of information was incomplete, omitting material facts and presenting other facts inaccurately. The Trustee, alluding to documents he had obtained from other sources, brought certain deficiencies to Alpha Prime's attention. The fund failed to adequately address most deficiencies. Although Alpha Prime allowed the term sheet to expire, it continued to demand that the Trustee engage in settlement discussions. In October 2013, with the Trustee concerned by Alpha Prime's efforts to omit and misrepresent material, the Trustee informed Alpha Prime that he could not continue to engage in settlement discussions.

Despite the unsuccessful end of the negotiations just months before, in February 2014, Alpha Prime's and Senator Fund's counsel asked the Trustee's counsel to consent to mediation. The funds' request contained no details about the scope of or the procedures for the mediation. When pressed for details, the funds' counsel confirmed he saw no need for further disclosure of information in connection with the proposed mediation. He refused to explain why the Trustee's claims against Alpha Prime and Senator Fund should be mediated together.

ARGUMENT

I. ALPHA PRIME'S AND SENATOR FUND'S MOTION SHOULD BE DENIED

Alpha Prime and Senator Fund can point to no authority that would allow them to strong-arm the Trustee to participate in mediation.

Mediation is "typically a voluntary process."[8] And "ultimately, [it] will only succeed if the parties themselves want it to, and a court's order to mediate . . . will not change the mind of [a] party who believes that settlement is not in their best interest."[9] A party cannot be coerced into settling or into making an offer to settle, by threat of sanction or otherwise.[10] Here, in light of the parties' extensive prior direct negotiations and the funds' obstruction of discovery, court-ordered mediation is an inappropriate method of proceeding.

Neither General Order M-390 of the United States Bankruptcy Court for the Southern District of New York[11] nor the Order (1) Establishing Litigation Case Management Procedures for Avoidance Actions and (2) Amending the February 16, 2010 Protective Order,[12] the two authorities to which Alpha Prime and Senator Fund point, would compel any different result.

General Order M-390 sets forth procedures under which the mediation of a bankruptcy case or an adversary proceeding could be conducted. It is not authority to compel mediation.[13] In light of the Trustee's good-faith settlement discussions with Alpha Prime and Senator Fund in the past, the Trustee believes that mediation prior to discovery would only waste resources.

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[8] *In re A.T. Reynolds & Sons, Inc.*, 452 B.R. 374, 381 (S.D.N.Y. 2011).

[9] *Id.* at 383.

[10] *Id.* at 382 (citing *Dawson v. United States*, 68 F.3d 886, 897 (5th Cir. 1995)).

[11] *In re: Adoption of Procedures Governing Mediation of Matters and the Use of Early Neutral Evaluation and Mediation/Voluntary Arbitration in Bankruptcy Cases and Adversary Proceedings.*

[12] *Sec. Inv. Protection Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff)*, Adv. Pro. No. 08-01789 (Bankr. S.D.N.Y. Nov. 10, 2010), ECF No. 3141.

[13] General Order M-390, Section 1.1.

The Order Establishing Litigation Case Management Procedures for Avoidance Actions governs only cases in which the Trustee "has not discovered evidence of lack of good faith."[14] It does not govern cases, as here, where there are allegations of inequitable conduct and lack of good faith, which would support the recovery of principal and the equitable subordination of the defendants' customer claims. The Avoidance Actions referred to in the Order do not require the determination of complex factual questions that the Trustee's cases against Alpha Prime and Senator Fund involve. Contrary to Alpha Prime's and Senator Fund's insinuation, the Order does not announce a general policy for mandatory mediation of a trustee's avoidance action upon the mere request of a defendant, regardless of the circumstances. Given the posture of this proceeding, mediation would be fruitless.

There are cases in which the Trustee will explore early settlement because of the benefit the settlement could confer upon the BLMIS customer property estate. Indeed, in this case, the Trustee repeatedly engaged with Alpha Prime and Senator Fund in direct negotiations. Those negotiations have proven, however, that early, pre-discovery settlement would likely not benefit the estate. Alpha Prime's and Senator Fund's motion should be denied.

CONCLUSION

For each of the foregoing reasons, Movants have failed to establish a basis for the entry of an order directing the parties to engage in mediation and their motion should be denied.

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[14] Trustee's Motion for Entry of an Order (1) Approving Litigation Case Management Procedures for Avoidance Actions and (2) Amending Global Protective Order, *Sec. Inv. Protection Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff),* Adv. Pro. No. 08-01789 (Bankr. S.D.N.Y. Oct. 21, 2010), ECF No. 3058 n.5 ("For the Avoidance Actions (the actions governed by the within proposed procedures), the Trustee, to date, has not discovered evidence of lack of good faith and will proceed under this presumption to limit recoveries sought to fictitious profits and preferences.").

Dated: New York, New York
March 18, 2014

Respectfully submitted,

s/ Geoffrey A. North

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